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March 14, 2006

AGENDA ITEM 5

TO: MEMBERS OF THE FINANCE COMMITTEE

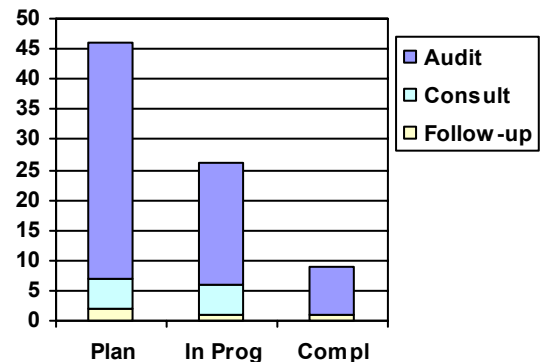
- I. **SUBJECT:** Quarterly Status Report
- II. **PROGRAM:** Audit Services
- III. **RECOMMENDATION:** Information only
- IV. **SUMMARY:**

In accordance with the Finance Committee's Audit Resolution Policy and Procedures, the Office of Audit Services presents its Quarterly Status Report of audit activity. The following provides the status of audits and special projects as of December 31, 2005.

1. Status of projects and activities in the Fiscal Year 2005 / 2006 Board approved annual Audit Plan

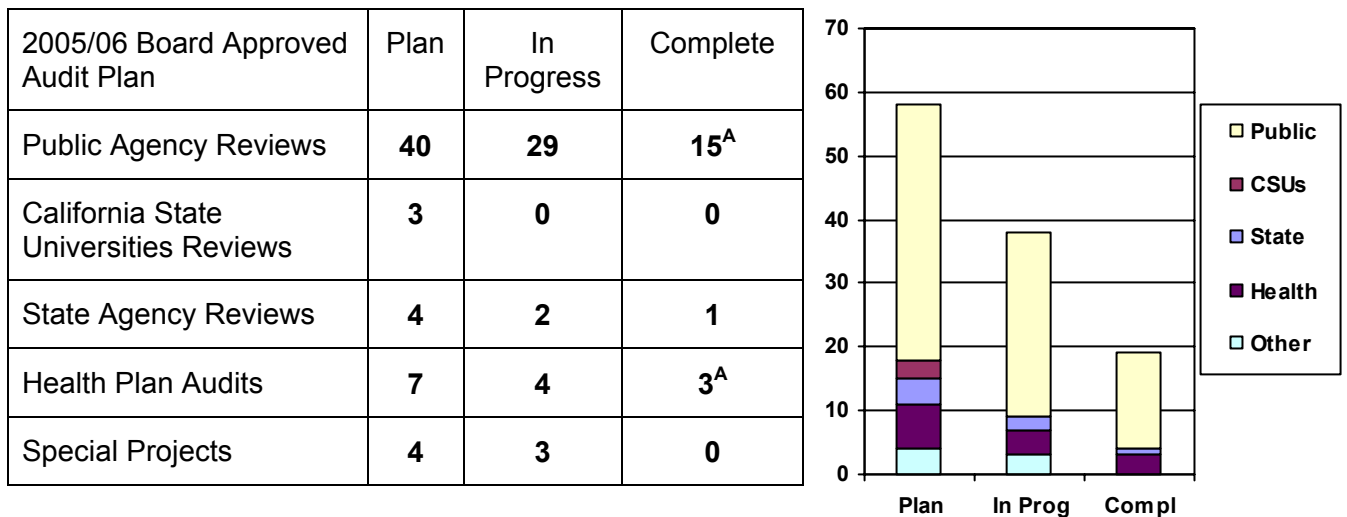
- A. Internal Audits – Internal audit projects and consulting assignments focus on compliance, and the effectiveness and efficiency of CalPERS operations, systems, policies, and procedures. Detail on these projects is provided on Attachment 1A.

2005/06 Board Approved Audit Plan	Plan	In Progress	Complete
Audit Projects	39	20	8 ^A
Consulting Projects	5	5	0
Audit Follow-up	2	1	1

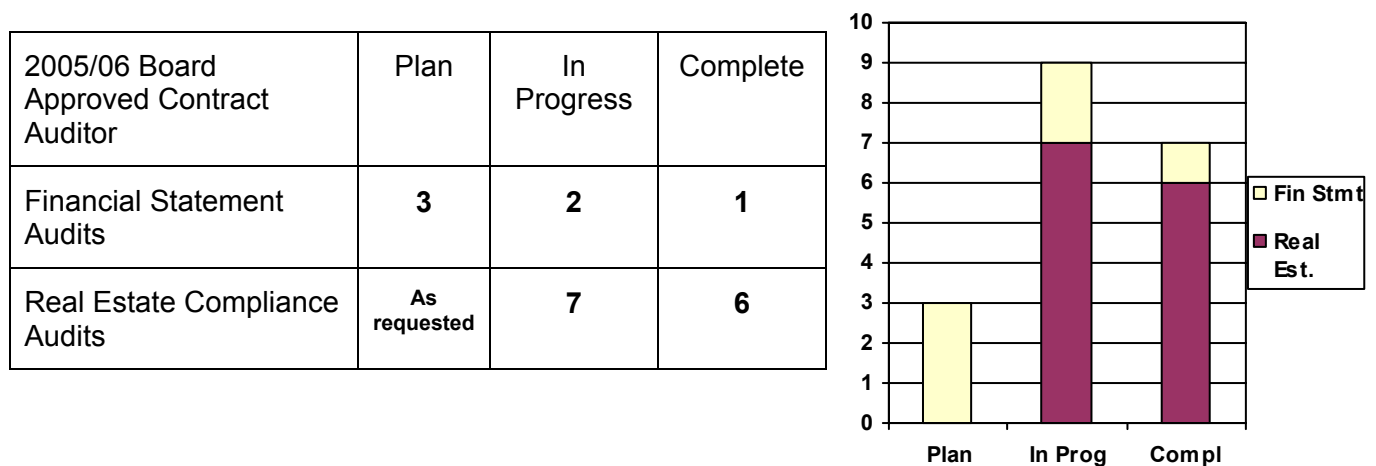


A – Includes projects that started in prior fiscal year as outlined in Attachment 1A.

B. Field Audits and Reviews— Field audits and reviews include compliance reviews of employer entities belonging to the System, audits of Health Maintenance Organizations contracting with the System, compliance audits of health care third-party administrators, and audits of external providers of investment-related services. Detail on these projects is provided on Attachment 1B.



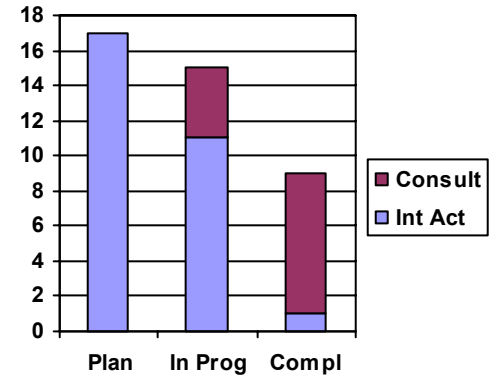
C. Contract Audits – Contract audits include audit work performed by external auditors. The number of real estate compliance audits is determined over the course of the fiscal year. Detail on these projects is provided on Attachment 1C.



A- Includes projects started in prior fiscal year as outlined in Attachment 1B.

D. Management Consulting Projects - In addition to the specific projects in the approved Audit Plan, during the year the Office of Audit Services responds to subsequent requests from the Board of Administration, Executive Management, and program divisions for audit and consulting projects. The approved Audit Plan includes an allocation of hours for these projects. Detail on these projects is provided in Attachment 1D.

Management Consulting Projects	Plan	In Progress	Complete
Management Consulting Projects	As requested	4	8
Office of Audit Services Internal Activities	17	11	1

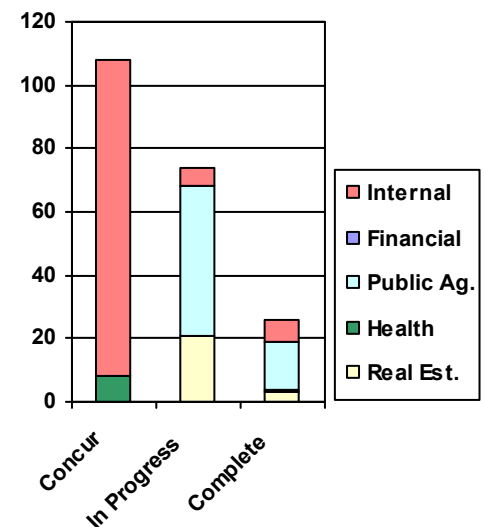


2. Findings / issues resulting from auditing work

A status of *Concur* indicates management has agreed with the finding and plans corrective action. *In Progress* indicates management is taking corrective action. *Complete* status indicates satisfactory resolution of the finding. *Unresolved* status indicates management does not agree with the finding or recommendation or has not taken adequate action; in such a case, the finding is referred to executive management for resolution.

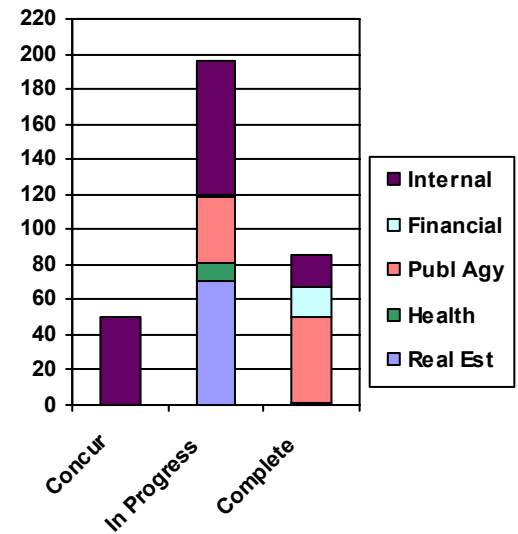
A. Findings / issues resulting from current year projects.

Activity	Concur	In Progress	Complete	Unresolved
Internal Audits	100	6	7	0
Financial/External Audits	0	0	0	0
Public Agency Reviews	0	47	15	0
Health Plan Audits	8	0	1	0
Real Estate Audits	0	21	3	0



B. Findings / issues resulting from prior years' projects.

Activity	Concur	In Progress	Complete	Unresolved
Internal Audits	50	76	19	0
Financial/External Audits	0	1	17	0
Public Agency Reviews	0	38	49	0
Health Plan Audits	0	10	1	0
Real Estate Audits	0	71	0	0



3. Findings / Issues

During the first half of Fiscal Year 2005/06, we completed 16 reviews of public contracting agencies. The most frequently reported issues were incorrect reporting of compensation, not enrolling eligible part-time employees, and payroll reporting errors. The following table is a summary of the findings included in the audit reports issued during the first half of Fiscal Year 2005/06.

Type of Finding – FY 2005/06	Number of Findings
Enrollment	13
Compensation	12
Payroll reporting errors	9
Contributions/payroll information not reported timely	7
Unused sick leave	6
Reinstatement of retired annuitants	6
Independent contractors	3
Industrial disability not made timely	2
Publicly available salary schedule not available	2
Payrate reporting error	2

Internal Audits

During the first half of Fiscal Year 2005/06, we completed eight internal audits focusing on enterprise risk to the organization. The areas of primary emphasis included financial accountability and internal control compliance, contracting and purchasing activities, Medicare transfer eligibility, and information technology controls. Key issues reported included the need for improved compliance with a number of aspects of State Administrative Manual internal control requirements, controls over the building manager's cash receipts and disbursements and bank reconciliations, controls over contracting and purchasing activities, notification and follow-up to members of their eligibility for Medicare, and key controls over system access. Detail on these issues is found on Attachment 2A – Internal, included in this agenda item.

Acceptance of Risk – Internal Audits

The Office of Audit Services reported two findings related to health care fund cash flow in a report dated May 2004. These are summarized on pages 7 and 8 of Attachment 2B – Internal Audits. These issues relate to processes under management of the Health Benefits Branch involving a mismatch between the time outgoing payments to health plans are due compared with incoming health premium contributions from contracting agencies.

Although management concurs with the audit observations, its assessment is that the current process sufficiently minimizes the gap between the payment due date to health plans and the date CalPERS receives payment from contracting agencies. Therefore, management of the Health Benefits Branch has decided to formally accept the risk associated with the observations.

Management Consulting Projects

The Office of Audit Services completed eight requests for management consulting projects in the first half of the fiscal year. Major projects included reconciliation assistance to Fiscal Services' Investment Accounting area, a major review of the fixed income management system trading compliance, assistance with the accountability for performance initiative, and a special review of certain benefit payments.

Audit Follow-Up

Consistent with the Audit Resolution Policy and Procedures, the Office of Audit Services worked with management to either resolve or develop corrective action plans for 86 audit issues more than one year old, with the result of resolution of a number of older outstanding issues. We report on the status of all these audit issues, including management's corrective action target dates, in Attachment 2B – Internal, included in this agenda item.

Health Plan Audits

We completed three audits of health plan contract compliance during the first half. These audits addressed HMO, pharmacy, and long-term care areas. The main issues identified in these audits include improved reporting of data to CalPERS and improved eligibility tracking. Detail on these audits is found on Attachment 2A – Health Plan Audits, included in this agenda item.

Financial Statement Audits

The external financial statement auditor, Deloitte and Touche, completed its audit of CalPERS' financial statements as of June 30, 2005, and presented an unqualified opinion at the November 2005 Finance Committee meeting. Deloitte presented a draft management letter summarizing all its findings and recommendations related to the financial statement audit at the February 2006 Finance Committee meeting. The issues presented by the auditor include lack of accounting reconciliations, lack of adequate accounting controls and processes for summarizing, recording, and disclosing accounting data, and certain information security concerns.

Real Estate Audits

The external real estate auditor completed six audits in the first half of Fiscal Year 2005/06. The most frequently reported issues, as in Fiscal Year 2004/05, continue to address insurance requirements, property condition, record keeping, various fee calculations, and competitive bidding. Detail on the real estate audits is found on Attachment 2A and 2B – Real Estate, included in this agenda item.

V. STRATEGIC PLAN:

This item is not a specific product of the strategic plan, but is required by the Finance Committee's Audit Resolution Policy and Procedures and the Office of Audit Services Charter.

VI. RISKS/COST:

This is an information item and does not result in any risks/costs. Staff is available to answer any questions that the Finance Committee may have.

Larry Jensen, Chief
Office of Audit Services

Peter H. Mixon
General Counsel